

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF MOCKINGBIRD VALLEY )  
SANITATION, INC. FOR A RATE ADJUSTMENT )  
PURSUANT TO THE ALTERNATIVE RATE FILING ) CASE NO. 94-034  
PROCEDURE FOR SMALL UTILITIES )

O R D E R

On January 31, 1994, Mockingbird Valley Sanitation, Inc. ("Mockingbird") filed its application for Commission approval of proposed sewer rates. Commission Staff, having performed a limited financial review of Mockingbird's operations, has prepared the attached Staff Report containing Staff's findings and recommendations regarding the proposed rates. All parties should review the report carefully and provide any written comments or requests for a hearing or informal conference no later than 15 days from the date of this Order.


IT IS THEREFORE ORDERED that all parties shall have no more than 15 days from the date of this Order to provide written comments regarding the attached Staff Report or requests for a hearing or informal conference. If no request for a hearing or informal conference is received, this case will be submitted to the Commission for a decision.

Done at Frankfort, Kentucky, this 18th day of April, 1994.

ATTEST:

  
Executive Director

PUBLIC SERVICE COMMISSION

  
For the Commission

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF MOCKINGBIRD )  
VALLEY SANITATION, INC. FOR A )  
RATE ADJUSTMENT PURSUANT TO ) CASE NO. 94-034  
THE ALTERNATIVE RATE FILING )  
PROCEDURE FOR SMALL UTILITIES )

STAFF REPORT

Prepared By: Mark C. Frost  
Public Utility Financial  
Analyst, Chief  
Water and Sewer Revenue  
Requirements Branch  
Financial Analysis Division

Prepared By: John Geoghegan  
Public Utility Rate  
Analyst,  
Communications, Water  
and Sewer Rate Design Branch  
Rates and Research Division

STAFF REPORT  
ON  
MOCKINGBIRD VALLEY SANITATION, INC.  
CASE NO. 94-034

A. Preface

On January 31, 1994, Mockingbird Valley Sanitation, Inc. ("Mockingbird") filed its application seeking to increase its rates pursuant to the Alternative Rate Filing Procedure for Small Utilities ("ARF"). Mockingbird's proposed rates would produce an increase in its annual revenues of \$4,374, an increase of 33.4 percent over test-period normalized revenues from rates of \$13,104.

In Order to evaluate the requested increase, the Commission Staff ("Staff") chose to perform a limited financial review of Mockingbird's operations for the test-period, the calendar year ending December 31, 1992. Since Mockingbird requested and received Staff assistance in preparing its ARF application, the field review was conducted prior to the filing of the application.

Mark Frost of the Commission's Division of Financial Analysis performed the limited review on January 15, 1993. Mr. Frost is responsible for the preparation of this Staff Report except for Section B, Operating Revenue; Section D, Rate Design; and Appendix A, which were prepared by John Geoghegan of the Commission's Division of Rates and Research. Based on the findings contained in this report, Staff recommends that Mockingbird be allowed to increase its revenues from rates by \$4,374.

### Scope

The scope of the review was limited to obtaining information to determine whether the test-period operating revenues and expenses were representative of normal operations. Insignificant or immaterial discrepancies were not pursued and are not addressed herein.

### B. Analysis of Operating Revenues and Expenses

#### Operating Revenues

Mockingbird reported operating revenue of \$11,882 in its 1992 Annual Report. Based on the end-of-period customer level and Mockingbird's current rate, the normalized revenue from rates would be \$13,104.<sup>1</sup> Therefore, Staff recommends that operating revenue be increased by \$1,222.

#### Operating Expenses

In its application, Mockingbird reported actual and pro forma test period operating expenses of \$16,805 and \$16,604, respectively. The following are Staff's recommended adjustments to Mockingbird's actual test period operations and discussions of Mockingbird's proposed pro forma adjustments:

Owner/Manager Fee: In the test period Mockingbird paid its owner/manager \$2,675 for the following services: mowing \$1,550;

---

<sup>1</sup> \$28 x 39 Customers x 12 Months = \$13,104.

maintenance \$625; and transportation \$500. Mockingbird proposed to replace the test period payments with a \$1,200 owner/manager fee.

Given the owner's responsibilities and duties, an owner/manager fee should be included in test period operations. The Commission has allowed sewer utilities of Mockingbird's size owner/manager fees of \$2,400, which is reasonable in this instance. Accordingly, Staff recommends that test period operations be reduced by \$275 to reflect the payment of a \$2,400 owner/manager fee.

Routine Maintenance Fee: Mockingbird proposed a pro forma level of routine maintenance fee expense of \$3,300, an increase of \$783 above its test period level. Mockingbird pays a routine maintenance fee of \$275 per month or \$3,300 annually, which is the basis for its adjustment.

Based upon its knowledge of the routine maintenance fees paid by comparable sewer utilities, Staff considers a fee of \$275 per month to be within a range that is reasonable and therefore, it should be reflected in test period operations. Staff recommends that routine maintenance fee expense be increased by \$783.

KPDES Testing Fee: Mockingbird proposed a pro forma level of KPDES testing fee expense of \$540, an increase of \$405 above its test period level. Mockingbird pays a KPDES testing fee of \$135 per quarter or \$540 annually, which is the basis for its adjustment.

Staff is of the opinion that the KPDES testing fee paid by Mockingbird is reasonable and should be reflected in test period operations. Therefore, KPDES testing fee expense has been increased by \$405.

Agency Collection Fee: Mockingbird's customer billing and collection is performed by the Oldham County Water District ("Oldham County") at a fee of \$2 per customer. This fee combined with the number of test period customers results in Mockingbird's proposed pro forma agency collection fee expense of \$936.<sup>2</sup>

Mockingbird's test period operating revenues were reported net of the collection and billing expense. Since the operating revenues recommended herein reflect the gross collections, Staff recommends that Mockingbird's adjustment be accepted and that test period operating expenses be increased by \$936.

Bookkeeping: Mockingbird proposed a pro forma level of bookkeeping expense of \$600, a decrease of \$500 from its test period amount. In the test period Mockingbird paid its bookkeeper a fee of \$100 per month. To control its operating costs, Mockingbird has proposed to decrease the fee to \$50 per month or \$600 annually.

Given that Mockingbird's billing and collection is performed by Oldham County and the small number of checks written in the test

---

<sup>2</sup> 39 End-of-Period Customers x \$2 x 12 Months = \$936.

period, Staff is of the opinion that a monthly bookkeeping fee of \$50 is reasonable. Accordingly, bookkeeping expense has been reduced by \$500.

Outside Services: Mockingbird pays its accountant \$250 to prepare its annual financial statements and tax returns. Mockingbird erroneously included its 1991 and 1992 accounting fees in the test period operations. To correct this error, Mockingbird proposed to decrease outside services expense by \$250. Upon review of the general ledger, Staff determined that Mockingbird's adjustment is correct and recommends that it be accepted.

Interest: Mockingbird has borrowed \$184,490 from Bertrand Schureck, its owner, to install the treatment plant, lift station, and fence. The outstanding indebtedness would result in a annual interest expense of \$18,161.<sup>3</sup>

Mockingbird was informed of the Commission's practice of allowing a dollar-for-dollar coverage of interest expense in the calculation of revenue requirement. A dollar-for-dollar coverage of interest expense would require Mockingbird's monthly sewer rate to increase by approximately \$39.<sup>4</sup> Because of the significant

| 3 | Loan                  |          | Interest           |                  |
|---|-----------------------|----------|--------------------|------------------|
|   | Purpose               | Date     | Calculation        | Expense          |
|   | Install Plant         | 8/31/82  | \$ 174,593 x 9.75% | \$ 17,023        |
|   | Lift Station          | 12/01/85 | \$ 4,786 x 11.5%   | 550              |
|   | Fence                 | 12/01/86 | \$ 5,110 x 11.5%   | + 588            |
|   | Total Annual Interest |          |                    | <u>\$ 18,161</u> |

<sup>4</sup> \$18,161 ÷ 39 Customers ÷ 12-Months = \$39.

impact interest expense would have on its monthly rate, Mockingbird chose not to ask for its recovery.

According to KRS 278.300 (1), "[n]o utility shall issue any securities or evidences of indebtedness, or assume any obligation or liability in respect to the securities or evidences of indebtedness of any other person until it has been authorized so to do by order of the commission." However, KRS 278.300 (8) states that this section is not applicable if the indebtedness has a 2 year term, and is renewed in aggregate for a total of no more than 6 years from the date of the original issuance.

Because Mockingbird's loans were due and payable in 1 year increments they would not have required prior Commission authorization. However, the 6 year renewal period has been exceeded thus requiring Commission approval. To date Mockingbird has not requested or received Commission authorization to incur its indebtedness to Mr. Schureck.

Given that Mockingbird's loans are not authorized by the Commission, Staff is in agreement with Mockingbird that the associated interest expense should be excluded for rate making purposes.

#### Operations Summary

Based on the recommendations of Staff contained in this report, Mockingbird's operating statement would appear as set forth in Appendix B to this report.



C. Revenue Requirements Determination

The approach frequently used by this Commission to determine revenue requirements for small, privately-owned utilities is the operating ratio. This approach is used primarily when a basis for rate-of-return determination does not exist or the utility plant investment has been depreciated or recovered through the receipt of contributions. Staff recommends the use of this approach in determining Mockingbird's revenue requirement.

Mockingbird requested additional revenue of \$4,374. Based on the Staff adjusted operating expenses and the operating ratio normally allowed by the Commission, Staff believes Mockingbird could justify additional revenue of \$7,676.<sup>5</sup> However, since Mockingbird's proposed rates will produce a positive cash flow of \$4,428,<sup>6</sup> Staff recommends that the proposed rates be accepted.

If Mockingbird chooses to amend its application to reflect rates that will generate the additional revenue of \$7,676 which

---

|              |   |    |              |
|--------------|---|----|--------------|
| <sup>5</sup> | \$17,804 Adjusted Operating Exp + 88% Ratio = | \$ | 20,232       |
|              | Less: Adjusted Operating Expenses             | -  | 17,804       |
|              | Net Operating Income                          | \$ | 2,428        |
|              | Times: Gross-up Tax Factor                    | x  | 1.2254902    |
|              | Subtotal                                      | \$ | 2,976        |
|              | Add: Adjusted Operating Expenses              | +  | 17,804       |
|              | Recommended Operating Revenue                 | \$ | 20,780       |
|              | Less: Normalized Operating Revenues           | -  | 13,104       |
|              | Potentially Justifiable Revenue Increase      | \$ | <u>7,676</u> |


|              |                               |     |              |
|--------------|-------------------------------|-----|--------------|
| <sup>6</sup> | Adjusted Net Operating Income | \$< | 4,700>       |
|              | Add: Requested Increase       |     | 4,374        |
|              | Depreciation Expense          | +   | 4,754        |
|              | Cash Flow                     | \$  | <u>4,428</u> |


Staff believes could be justified, it should do so when filing comments to the Staff Report. In the event that Mockingbird does request rates that differ from those previously noticed to customers, it should be required to re-notice its customers of the new proposed rates.

D. Rate Design

Mockingbird has proposed no change to its rate design. Staff is of the opinion that the current flat monthly rate design is appropriate for Mockingbird. Therefore, any change in revenue will be added to or subtracted from Mockingbird's existing rate structure. Appendix A outlines the recommended rates based on the revenue increase recommended herein.

E. Signatures

  
Prepared By: Mark C. Frost  
Public Utility Financial  
Analyst, Chief  
Water and Sewer Revenue  
Requirements Branch  
Financial Analysis Division

  
Prepared By: John Geoghegan  
Public Utility Rate  
Analyst, Principal  
Communications, Water and  
Sewer Rate Design Branch  
Rates and Research Division

APPENDIX A

Mockingbird Valley Sanitation

The following rate is recommended for Mockingbird Valley Sanitation:

|              |         |
|--------------|---------|
| Monthly Rate | \$37.35 |
|--------------|---------|

APPENDIX B  
TO THE STAFF REPORT CASE NO. 94-034

|                          | <u>Actual<br/>Operations</u> | <u>Pro Forma<br/>Adjustments</u> | <u>Pro Forma<br/>Operations</u> |
|--------------------------|------------------------------|----------------------------------|---------------------------------|
| Operating Revenue:       |                              |                                  |                                 |
| Residential              | <u>\$ 11,882</u>             | <u>\$ 1,222</u>                  | <u>\$ 13,104</u>                |
| Operating Expenses:      |                              |                                  |                                 |
| Owner/Manager Fee        | \$ -0-                       | \$ 2,400                         | \$ 2,400                        |
| Sludge Hauling           | 1,418                        | -0-                              | 1,418                           |
| Electric                 | 2,159                        | -0-                              | 2,159                           |
| Mowing Fee               | 1,550                        | < 1,550>                         | -0-                             |
| Routine Maintenance Fee  | 2,517                        | 783                              | 3,300                           |
| KPDES Testing            | 135                          | 405                              | 540                             |
| Maintenance              | 1,341                        | < 625>                           | 716                             |
| Agency Collection Fee    | -0-                          | 936                              | 936                             |
| Office Supplies          | 13                           | -0-                              | 13                              |
| Telephone                | 510                          | -0-                              | 510                             |
| Bookkeeping              | 1,100                        | < 500>                           | 600                             |
| Accounting               | 500                          | < 250>                           | 250                             |
| Transportation           | 600                          | < 600>                           | -0-                             |
| Depreciation             | 4,754                        | -0-                              | 4,754                           |
| Taxes Other Than Income  | <u>208</u>                   | <u>-0-</u>                       | <u>208</u>                      |
| Total Operating Expenses | <u>\$ 16,805</u>             | <u>\$ 999</u>                    | <u>\$ 17,804</u>                |
| Net Operating Income     | <u>\$&lt; 4,923&gt;</u>      | <u>\$ 223</u>                    | <u>\$&lt; 4,700&gt;</u>         |